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No. 03-790

IN THE

Supreme Court of the United States

SAFETY NATIONAL CASUALTY CORPORATION,

Petitioner,

v.

DOW CORNING CORPORATION,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

REPLY BRIEF

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STATEMENT UNDER RULE 29.6

Petitioner's corporate disclosure statement was set forth at page *ii* of its Petition for a Writ of Certiorari, and there are no amendments to that statement.

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REPLY

I. The Eighth Circuit's Decision Conflicts With The Court's Arbitration Precedent: An Arbitrator, And Not The Court, Decides What Kind Of Arbitration Proceeding The Parties Have Agreed To, Including All Procedural Matters Affecting The Arbitration's Final Disposition.

Dow Corning's Brief in Opposition is telling. Dow Corning spends pages addressing the distinction between binding and non-binding arbitration[1], but never addresses the central issue presented by Safety's Petition, namely, the conflict between the Eighth Circuit's decision and the Court's decision in *Green Tree Fin. Corp. v. Bazzle*, __ U.S. __, 123 S. Ct. 2402 (2003). Moreover, Dow Corning does not touch upon the prevalence of Safety's arbitration clause in the insurance field or how the Eighth Circuit's decision will disrupt the final and binding resolution of disputes through arbitration by opening up the courts to challenges by "losers" who will contend that arbitration is nothing more than a non-binding prelude to litigation.

The reason for Dow Corning's silence is simple. The Eighth Circuit's decision cannot survive *Green Tree*, the Court's most recent arbitration precedent.

In *Green Tree*, the Court distinguished between questions of arbitrability – which are for a court to decide – and questions of substance and arbitration procedure – which are for an arbitrator to decide. The Court has narrowly defined the question of arbitrability as whether the parties agreed in their contract to arbitrate a particular dispute. *AT&T Technologies, Inc. v. Communication Workers*, 475 U.S. 643, 649 (1986). The Court has emphasized the question is one of "limited scope" and applies to "gateway" matters only. *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 83 (2002). The question concerns the validity of an arbitration clause or its application to an underlying dispute. *Green Tree*, 123 S. Ct. at 2407.

1. Safety freely acknowledges the distinction.

Arbitrability, however, does not embrace matters of contract interpretation and arbitration procedure. *Id.* Nor does arbitrability address "what *kind of arbitration proceeding* the parties agreed to." *Id.* (emphasis in original). These questions are reserved for the arbitrator to decide. Once a court concludes a dispute is arbitrable, all other questions are for the arbitrator to resolve, including procedural questions that grow out of the dispute and which affect its "final disposition." *Howsam*, 537 U.S. at 84 (citing *John Wiley & Sons, Inc. v. Livingston*, 376 U.S. 543, 557 (1964)).

The "final and binding" issue, which the arbitrators decided in this case, is not a question of arbitrability. The issue concerns what kind of arbitration proceeding the parties agreed to and constitutes a matter of contract interpretation and arbitration procedure. *Green Tree*, 123 S. Ct. at 2407. As a procedural question affecting the "final disposition" of the parties' dispute, it was a matter reserved for the arbitrators' exclusive determination. *Howsam*, 537 U.S. at 84. The Court's arbitration jurisprudence permits no other conclusion.

Contrary to Dow Corning's argument, the parties did agree to submit the binding/non-binding issue to the arbitrators. Brief in Opp. 14-19. This determination did not exceed the arbitrators' authority. Dow Corning and Safety agreed to arbitrate *any* dispute arising out of the policies. Pet. App. 4a-5a. Whether the policies called for binding or non-binding arbitration was a matter of contract interpretation and arbitration procedure that arose from the policies. It was rightly decided by the arbitrators.

The Court has stated quite plainly that matters of procedure lie solely within the arbitrator's discretion. *John Wiley & Sons, Inc.*, 376 U.S. at 557. As reaffirmed by the Court in *Green Tree*, "[a]rbitrators are well situated to answer" questions of contract interpretation and arbitration procedure. 123 S. Ct. at 2407. Moreover, "[t]he [FAA] establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself" or a defense

to arbitrability. *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983). This is true even where the scope of the arbitration clause is ambiguous. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 62 (1995).

This case was not one where the arbitrators exceeded their authority by resolving a dispute that was not subject to a valid arbitration agreement. Rather, they decided a question of procedure and contract interpretation, which rests within their exclusive province.

A. Questions Of Contract Interpretation And Arbitration Procedure Are For The Arbitrator To Decide.

In opposition, Dow Corning invites the Court to engage in contract interpretation to decide the "final and binding issue," a procedural question addressing the "final disposition" of the parties' dispute. Brief in Opp. 12-14. Contrary to Dow Corning's argument and the Eighth Circuit's decision, the issue is not controlled by the Court's decision in *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995). Brief in Opp. 12, 17. Dow Corning's reliance on *First Options* is misplaced and confuses the nature of an arbitrability determination. Unlike this case, *First Options* involved a "gateway" question of arbitrability, namely, whether the parties had agreed to arbitrate the issue of arbitrability. 514 U.S. at 942.

Here, there is no dispute that Dow Corning and Safety had agreed to arbitrate any disputes arising out of the insurance policies. Pet. App. 4a-5a. Before this Court, Dow Corning does not argue otherwise.

Instead, Dow Corning presses the Court to construe the arbitration provision, as did the Eighth Circuit, and find that the parties' agreement did not provide for binding arbitration. Brief in Opp. 11-12. However, on a procedural question involving matters of contract interpretation, a court has no role. *Green Tree*, 123 S. Ct. at 2407; *John Wiley & Sons, Inc.*, 376 U.S. at 557. A reviewing court must affirm an arbitration award

so long as the arbitrators are even arguably construing or applying the contract and acting within the scope of their authority. *United Paperworkers Intern'l Union, AFL-CIO v. Misco, Inc.*, 484 U.S. 29, 38 (1987). Indeed, a reviewing court must affirm even if it is convinced the arbitrators have "committed serious error." *Id.*

B. The Phrase "Condition Precedent" Does Not Provide For Non-Binding Arbitration.

Dow Corning's focus on the "condition precedent" language in the arbitration clause does not compel a different conclusion. Brief in Opp. 10, 13. The arbitrators correctly construed the language in light of the circumstances surrounding its drafting. "While this language might be unartful and anachronistic, it does not denote non-binding arbitration." *McKee v. Home Buyers Warranty Corp. II*, 45 F.3d 981, 986 (5th Cir. 1995). Instead, the phrase applies to the confirmation process permitted by 9 U.S.C. § 9 or to other litigation in which the arbitration would be final, but part of a larger litigation context. *Rainwater v. National Home Ins. Co.*, 944 F.2d 190, 194 (4th Cir. 1991); *McKee*, 45 F.3d at 985-86.

In *Rainwater*, the arbitration clause contained "condition precedent" language like Safety's policies: "The voluntary dispute settlement process provided herein shall be a *condition precedent to the commencement* of any litigation by any party to compel compliance with the warrant documents or to seek relief for any dispute arising out of this program." 944 F.2d at 192 (emphasis added). The Fourth Circuit disposed of the argument that the "condition precedent" language meant non-binding arbitration, explaining:

> Though NHIC's claim has some surface appeal, we think that the "condition precedent" language cannot carry all the weight NHIC would ascribe to it. Traditionally, federal courts were hostile to arbitration clauses since it was thought they could be avoided at the whim of either party. As a result,

> parties frequently included "condition precedent" language to make certain that the arbitration process ran its course before a federal court could entertain a suit. *Therefore, we read "condition precedent" to some extent as an artifact left over from the days of hostility toward arbitration. To the extent that the phrase has meaning, we find that it does not undermine the binding nature of arbitration*, but instead applies to the confirmation process permitted by 9 U.S.C. § 9, or to other litigation in which the arbitration award would be final but just a sub-text in some larger litigation context.

944 F.2d at 194 (citations omitted) (emphasis added).

The Fifth Circuit is in accord. In *McKee*, the arbitration clause provided: "The dispute settlement process *shall precede any litigation* attempted by either party on items that are specifically included in this warranty." 45 F.3d at 983 n.2 (emphasis added). The Fifth Circuit rejected the argument that this language made the parties' arbitration non-binding:

> We think this "federal policy favoring arbitration" covers more than simply the substantive scope of the arbitration clause – i.e., whether the Kilpatricks' claims were properly submitted to arbitration – and encompasses an expectation that such procedures will be binding. As a matter of federal law, the language of the warranty agreement is not sufficiently specific to call for non-binding arbitration.

Id. at 985.

These authorities demonstrate the arbitration clause in Safety's policies confirmed the parties' intent to resolve their disputes by binding arbitration. The "condition precedent" language, which was written in the years when many jurisdictions were still hostile to arbitration as an alternative to litigation, does not express the parties' intention to engage in a

"non-binding" process. In the context of an insurance coverage dispute arising from a complex mass tort, a non-binding process taking many years to resolve would be a great waste of money and energy if the exercise decided nothing and was merely a prelude to litigation. Read in context, the language "condition precedent to any right of action" refers to the "offensive" use of an arbitration award, *i.e.*, execution on or the enforcement of a money judgment, and does not constitute an agreement to engage in non-binding arbitration.

Contrary to Dow Corning's argument, the absence of words specifying "final and binding" arbitration is of no import. Brief in Opp. 11. Magic words are not necessary to make an arbitration binding. *Rainwater*, 944 F.2d at 193. Rather, in the case of a non-binding procedure, the opposite is true. There must be specific language in the agreement that calls for non-binding arbitration. *McKee*, 45 F.3d at 985. In the absence of such language, the expectation is that the arbitration will be binding. *Id.*

This is true here. There is no express language providing for non-binding arbitration in Safety's policies.

Dow Corning's attempt to distinguish *Rainwater* and *McKee* on the ground the arbitration clauses in those cases incorporated American Arbitration Association rules does not advance its position. Brief in Opp. 9-10. Safety's clause had a similar provision. In deciding the case, the arbitrators were bound to make their "decision with regard to the custom and usage of the insurance and reinsurance business." Pet. App. 5a. The agreement's incorporation of insurance and reinsurance custom and usage is indistinguishable from those agreements that incorporate American Arbitration Association rules. The fact there was no custom and usage evidence in the record is irrelevant. The insurance custom and usage were self-proving. By unanimously finding the arbitration binding, the three arbitrators necessarily followed insurance and reinsurance

custom and usage, of which they were experts.[2] Pet. App. 5a. The board's members were "active or retired, disinterested officials of insurance or reinsurance companies." *Id.*

Dow Corning's invitation to construe the arbitration agreement against Safety because it was the drafter should also be rejected. Brief in Opp. 13 n.7. The Court's precedent makes plain that matters of contract interpretation are for an arbitrator to decide. *Green Tree*, 123 S. Ct. at 2407. Moreover, this case is not one in which the rule of *contra proferentem* is applicable. The rule does not apply to sophisticated contractors, including corporations of immense size that are managed by professionals and guided by counsel on the same level as the insurer. *Eagle Leasing Corp. v. Hartford Fire Ins. Co.*, 540 F.2d 1257, 1261 (5th Cir. 1976); *Koch Engineering Co., Inc. v. Gibraltar Cas. Co.*, 878 F. Supp. 1286, 1288 (E.D. Mo. 1995), *aff'd*, 78 F.3d 1291 (8th Cir. 1996) (applying Missouri law).

C. Dow Corning's Authorities Are Immaterial To The Question Presented.

Dow Corning's recitation of authorities addressing non-binding procedures does not compel a contrary conclusion. Brief in Opp. 5-9. A cursory review of these authorities demonstrates they are inapplicable on their face.

The Court should declare, consistent with decisions by the Fourth, Fifth, and Tenth Circuits, that binding arbitration is presumed, absent specific language demonstrating that the parties intended a non-binding proceeding. There is a presumption of binding arbitration under the FAA, absent a clear indication that the parties intended a non-binding process. *Rainwater*, 944 F.2d at 192-94; *McKee*, 45 F.3d at 985; and

2. Even the arbitrator who ruled for Dow Corning on the merits joined the other two arbitrators in concluding the arbitration was binding. Pet. App. 86a, 89a. Similarly, in *Shook & Fletcher Asbestos Settlement Trust v. Safety Nat'l Cas. Corp.*, No. 03-1092, 2003 WL 22391526 (8th Cir. Oct. 21, 2003), a different thee-member arbitration panel concluded their award was binding, although the panel's decision on certain coverage issues was not unanimous.

P & P Indus., Inc. v. Sutter Corp., 179 F.3d 861, 866 (10th Cir. 1999). *See also Wabash Ry. Co. v. American Refrigerator Transit Co.*, 7 F.2d 335, 351 (8th Cir. 1925) (arbitration carries with it "an implied agreement to be bound").

In this case, the Eighth Circuit observed that binding arbitration is the norm under the FAA. Pet. App. 9a. Indeed, one circuit has concluded that non-binding proceedings fall outside the FAA's confines, holding where the dispute resolution process is not final and binding, the process is removed "from the warmth of the FAA blanket." *Dluhos v. Strasberg*, 321 F.3d 365, 372 (3d Cir. 2003).

Consider now the cases cited by Dow Corning. Dow Corning's leading authority, *United States v. Bankers Ins. Co.*, 245 F.3d 315 (4th Cir. 2001), an action brought by the Federal Emergency Management Agency against an insurer that sold and administered flood insurance policies for violations of the False Claims Act, amongst other claims, does not support its position. Brief in Opp. 5-6. The decision is inapposite. As pointed out by the Fourth Circuit, the National Flood Insurance Act, "specifically precludes arbitration that is binding on the Government." *Id.* at 321, *citing* 42 U.S.C. § 4083(b).

No similar expression of federal policy applies to the contracts between Dow Corning and Safety. The Fourth Circuit's decision in *Bankers Ins. Co.* does not call into question its decision in *Rainwater*, in which the same court held there is a "presumption that one submits to arbitration, . . . , precisely *because of* the binding quality of the process." 944 F.2d at 192 (emphasis in original). Indeed, the congressional policy that underlies this case is the very opposite of the one addressed in *Banker Ins. Co.* That policy favors and encourages arbitration precisely because it is a speedy, inexpensive, and efficient way to resolve disputes without litigation. *Rainwater*, 944 F.2d at 192.

Dow Corning's citation to *Wolsey, Ltd. v. Foodmaker, Inc.*, 144 F.3d 1205 (9th Cir. 1998), is equally irrelevant. Brief in Opp. 6. Unlike this case, *Wolsey, Ltd.*, involved a contract that expressly provided for non-binding arbitration. 144 F.3d at 1207.[3]

Similarly, Dow Corning's citation to cases decided by this Court does not advance its position or eliminate the conflict between the Eighth Circuit's decision and the Court's most recent arbitration precedent. Brief in Opp. 7-8. Two cases, *Chicago Teachers Union, Local No. 1, AFT, AFL-CIO v. Hudson*, 475 U.S. 292 (1986), and *Air Line Pilots Ass'n v. Miller*, 523 U.S. 866 (1998), concern the rights of *nonunion members* to challenge the calculation and collection of agency shop fees. These cases have no application here. Unlike this case, the nonunion employees were not parties to the agreements that prescribed the arbitration procedure to resolve their fee disputes; therefore, the nonunion employees never submitted to the arbitration process as their exclusive means of redress.

Dow Corning's citation to *Ortiz v. Fibreboard Corp.*, 527 U.S. 815 (1999), and *Bartnicki v. Vopper*, 532 U.S. 514 (2001), is likewise deficient. Brief in Opp. 8. Both cases concern agreements that expressly provided for non-binding arbitration.

Finally, Dow Corning's reference to alternative dispute resolution under 28 U.S.C. §§ 654-657 does not govern the federal policy for binding arbitration under the FAA. Brief in Opp. 8. The arbitration procedures enacted by Congress are consensual and specifically provide for a trial *de novo* in the district court. 28 U.S.C. §§ 654(b)(1), 657(c). Therefore, these procedures supply no guidance for review of an agreement subject to the FAA, which provides that any dispute arising out of the parties' contracts shall be submitted to a board of arbitration. Pet. App. 4a-5a.

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3. To the extent *Wolsey, Ltd.*, holds the FAA applies to non-binding proceedings, it is in conflict with the Third Circuit's decision in *Dluhos v. Strasberg*, 321 F.3d 365, 371-72 (3d Cir. 2003).

CONCLUSION

Certiorari in necessary to resolve the conflict between the Eighth Circuit's decision and the Court's arbitration precedent. Contrary to the Eighth Circuit's decision, once "gateway" issues of arbitrability are resolved in favor of arbitration, all other matters of contract interpretation and arbitration procedure are for an arbitrator – and not the court – to decide, including questions affecting the arbitration's final disposition. *Green Tree*, 123 S. Ct. at 2407; *Howsam*, 537 U.S. at 84. These are issues arbitrators "are well situated to answer." *Green Tree*, 123 S. Ct. at 2407. They are not reserved for a court to decide.

Moreover, by creating an "insurance" exception to the presumption that binding arbitration is the norm, the Eighth Circuit has destroyed the efficacy of arbitration clauses in insurance policies and reinsurance contracts, many of which provide that arbitration is a "condition precedent" to litigation. Pet. App. 6a. Although Dow Corning and Safety agreed to arbitrate any dispute arising out of their contracts, their arbitration has become nothing more than an expensive and time-consuming prelude to litigation. Because of the Eighth Circuit's decisions in this case and *Shook & Fletcher Asbestos Settlement Trust v. Safety Nat'l Cas. Corp.*, No. 03-1092, 2003 WL 22391526 (8th Cir. Oct. 21, 2003), other parties to insurance policies and reinsurance treaties must question whether they can rely on arbitration as an efficient and expeditious procedure to resolve their disputes without recourse of litigation. Therefore, the writ of certiorari should issue.

Respectfully submitted,

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